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In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 86

UNITED STATES OF AMERICA, PETITIONER

v.

ACME PROCESS EQUIPMENT COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the Court of Claims (R. 78) is reported at 347 F. 2d 509. Its findings (R. 123) are unreported. The opinion (R. 1) and findings [1] of the Commissioner of the Court of Claims are unreported.

JURISDICTION

The opinion of the Court of Claims (which includes its order, R. 123) was issued on June 11, 1965, and a timely motion for reconsideration denied on October 15, 1965 (R. 237). By orders of the Chief Justice

[1] Excerpts from the Commissioner's findings of fact are set forth at R. 62–77.

and Mr. Justice Brennan, entered on January 12, 1966, and February 9, 1966, the time for filing a petition for a writ of certiorari was extended to and including March 14, 1966 (R. 238–239). The petition for a writ of certiorari was filed on that day and granted on April 25, 1966 (R. 240, 384 U.S. 917). The jurisdiction of this Court is conferred by 28 U.S.C. 1255(1).

QUESTIONS PRESENTED

1. Whether the discovery that executives of a prime government contractor had accepted bribes from subcontractors in violation of the Anti-Kickback Act justified the government in terminating the prime contract.

2. Assuming that this was not adequate cause for termination and that the government therefore breached the contract, whether the contractor was entitled to restitution of the reasonable expenses he incurred under the contract, although the result (since the contract was not a profitable one for him) is to place him in a far better position than he would have occupied had the contract not been terminated.

STATUTE INVOLVED

Section 1 of the Anti-Kickback Act, 60 Stat. 37, as amended, 74 Stat. 740, 41 U.S.C. 51, provides in pertinent part:

> The payment of any fee, commission, or compensation of any kind or the granting of any gift or gratuity of any kind, either directly or indirectly, by or on behalf of a subcontractor, * * * (1) to any officer, partner, employee, or agent of a prime contractor holding a negotiated contract entered into by any de-

partment, agency, or establishment of the United States for the furnishing of supplies, materials, equipment or services of any kind whatsoever; * * * as an inducement for the award of a subcontract or order from the prime contractor * * * is prohibited. The amount of any such fee, commission, or compensation or the cost or expense of any such gratuity or gift, whether heretofore or hereafter paid or incurred by the subcontractor, shall not be charged, either directly or indirectly, as a part of the contract price charged by the subcontractor to the prime contractor * * *. The amount of any such fee, cost, or expense shall be recoverable on behalf of the United States from the subcontractor or the recipient thereof by setoff of moneys otherwise going to the subcontractor either directly by the United States, or by a prime contractor under any contract or by an action in an appropriate court of the United States. Upon a showing that a subcontractor paid fees, commissions, or compensation or granted gifts or gratuities to an officer, partner, employee, or agent of a prime contractor * * * in connection with the award of a subcontract or order thereunder, it shall be conclusively presumed that the cost of such expense was included in the price of the subcontract or order and ultimately borne by the United States. * * *[2]

Section 4 of the Act provides:

Any person who shall knowingly, directly or indirectly, make or receive any such prohibited

[2] Prior to its amendment in 1960, 74 Stat. 740, the Act applied only to contracts "on a cost-plus-a-fixed-fee or other cost reimbursable basis." 60 Stat. 37. See Statement, *infra*, pp. 9–10.

payment shall be fined not more than $10,000 or be imprisoned for not more than two years, or both.

STATEMENT

1. THE FACTS

A. THE CONTRACT AND ITS TERMINATION

On January 27, 1953, the Army Ordnance Corps awarded the Acme Process Equipment Co. a contract for the manufacture of 2,751 75 mm. recoilless rifles (F. 13, R. 132).[3] Acme had not previously manufactured weapons, but desired to diversify into the military supply field in order to offset unevenness in its civilian business (F. 2, R. 124). It was awarded the contract primarily because it was the lowest bidder. Its bid was $337.23 per rifle; the competing bids ranged from $423 to $930.16 (F. 7, R. 126–127). In addition, the government desired to encourage the entry of a new competitor into the field (F. 10, R. 130–131). The government contracting officers were, however, concerned over Acme's ability to produce the rifle at its bid price, especially since it did not have previous experience in the field. Acme was offered the opportunity to withdraw its bid, but declined, and the contract was then awarded to it (F. 7, 10, 13, R. 126–127, 130–131, 132–133).

It was contemplated that the project would largely be subcontracted, "leaving for Acme only the final finishing and assembly of components, and the earlier job of fashioning the rifle barrels from rough forg-

[3] "F." refers to the Findings of the Court of Claims (R. 123–237).

ings with machines furnished by the Government under a separate facilities contract" (R. 79). Indeed, the price of the subcontract with All Metals Industries—$300,000—was almost one third the total contract price of $1.04 million (F. 13, 61 R. 132, 232), and All Metals participated in some of the negotiations over the prime contract (F. 19, R. 139). In assessing the feasibility of Acme's bid, the Army reviewed Acme's subcontracting plans (F. 10, R. 130), and, during the final stages of negotiation, Acme advised the Army of changes in those plans (F. 11, R. 131). The contract itself required Acme to obtain the approval of the government for all subcontracts of more than $25,000 (R. 257).

The contract proved unprofitable to Acme, in part because of Acme's inexperience (F. 41, R. 187–188). Its cost of production on initial deliveries was more than double the ceiling price specified in the contract (F. 52 (a), (c), R. 206, 207–208).[4] Although delivery schedules were extended, Acme fell behind and liquidated damages were assessed (F. 14, 46, R. 133, 199–200). By the end of July 1954, 1,163 rifles had been delivered (F. 14, R. 133) at an average cost of $877.77 per rifle.[5] The government paid for the rifles, as they were delivered, at the contract price (R. 64, 68, 255).

On July 22, 1954, shortly after learning that employees of Acme had received kickbacks from several

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[4] The contract price of $337.23 per rifle was subject to redetermination up to $384.95 (F. 7, 13, R. 126, 132).

[5] This figure is based on the average costs of $1,179.29 for the first 446 and $690.21 for the remaining 717 rifles actually delivered (R. 110).

subcontractors (pp. 7–10, *infra*), the Army suspended the contract, and, a month later, cancelled it for "statutory violations" (F. 47, 49, R. 201, 202–204.) [6]

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[6] In addition to the kickbacks, the Army found that Acme had violated the False Claims Act (31 U.S.C. 231) and was guilty of conspiracy and common-law fraud (F. 49, R. 200–203). The Army also determined that there had been violation of Acme's contractual and statutory warranty against contingent-fee arrangements (10 U.S.C. 2306(b)). These contingent fee arrangements, like the kickbacks, involved Tucker and Norris (see *infra*, pp. 7–10). Acme hired Tucker in October 1952 to solicit bid invitations from private firms and the government. It agreed to pay him a commission of 5 percent on resulting gross weekly sales up to $10,000 and 3 percent of sales over $10,000. Tucker agreed to split this commission with Norris. In its original bid, which was submitted by Norris as General Manager of Acme's Defense Work Department, and later, on December 18, 1952 (one month before award of the prime contract), Acme executed government forms which represented that Acme "has not employed or retained a company or person (other than a full-time employee) to solicit or secure this proposed Contract" (F. 5, 8(a), R. 125–126, 127). Subsequently, on March 2, 1953, Acme hired Tucker and Norris on a full-time basis, with part of their compensation dependent upon the receipts of the plant at which the government contract was to be performed. On May 18, 1953, in response to a question as to Tucker's status, Acme stated that he had been originally hired on a part-time commission basis, but as of "January 1953" (*i.e.*, the time Acme's contract was executed) had entered upon full-time, non-commission employment (F. 8(f), 9, R. 129–130). The fact that Acme had been in violation of its contractual warranty against contingent fees for at least the first two months of its performance of the contract was not disclosed in the letter (F. 8(f), R. 129).

While the Court of Claims affirmed the Army's determination that both the False Claims Act and the contingent-fee warranty had been violated, it held that neither violation afforded a ground for termination of Acme's contract. As to the contingent-fee violations, the court held that the govern-

B. THE KICKBACKS

In October 1952, prior to the negotiation of the contract with the Army, Acme had hired Harry Tucker, Jr., and his associate, James Norris, for the purpose of establishing and managing a new division of the company to handle government contracts. Norris was made general manager of production, with authority to submit bids, sign government contracts, and award subcontracts; Tucker was placed in charge of sales, government contracts, and expediting subcontract operations (F. 3, 16, R. 124–125, 138).

Before the execution of the prime contract Tucker entered into arrangements with three companies, under which he was to receive "commissions" (which he shared with Norris) on sales by these companies to customers procured by Tucker, including Acme (F. 18, 22, 23, R. 139, 144–146).[7] After entering into this "kickback" arrangement, one of these companies—All Metals Industries, Inc.—participated in negotiation conferences between Acme and the Army which led to the award of the prime contract (F. 19, R. 139).

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ment's delay in cancelling after learning of the violations justified enforcement of the contract (R. 83–87). As to the False Claims Act, the court found that the government had not shown intent to defraud, and that such intent was necessary to justify nonenforcement on this ground (R. 102). We did not seek review of these aspects of the decision below.

[7] Tucker's contract with Foley Machine Company was limited to orders procured by Tucker from Acme (F. 23, R. 146). This contract was executed three days before the date of Acme's prime contract with the Army (F. 13, R. 132). Tucker's other two kickback contracts—signed in October and November 1952—were with All Metals Industries, Inc., and Manalapan Machine & Welding Works, and applied to any customer Tucker might bring in (F. 18, 22, R. 139, 144–145).

Within a few weeks after the award of the prime contract, all three companies were awarded subcontracts by Acme (F. 18, 19, 22, 23, R. 139–141, 144–146). A fourth company obtained subcontracts from Acme with the help of Tucker's father, with whom the company had a commission agreement (F. 24, R. 146–147), and a fifth obtained an Acme subcontract upon the recommendation of Philip Chagnon, who was on Acme's payroll as Norris' assistant. This company had a kickback agreement with Chagnon (F. 25, R. 147).

Within a month after the award of the prime contract, Jack Epstein, the superintendent of an Acme plant and the son of Acme's president and principal stockholder, joined the kickback conspiracy. Epstein and Tucker threatened cancellation of one of the subcontracts unless the subcontractor paid them $25,000. It was arranged that $23,500 would be paid to a dummy corporation owned by Tucker, Norris and Epstein for fictitious consulting services, and this amount was charged to Acme through an increase in the subcontract price (F. 1, 20, 21, R. 123–124, 141–144).[8]

Other officials of Acme were not consciously aware of the kickback activities of Epstein, Tucker, Norris and Chagnon until the late summer and fall of 1953 (F. 30, R. 149). However, Tucker's employment contract with Acme specifically stated that he represented and would continue to represent firms in other lines

[8] After the commencement of an official investigation of Norris' activities Tucker attempted to reverse the charge so that Acme would not bear the cost of the kickback (F. 21, R. 142–144).

of business and Acme did not consult with any of his other clients at the time Tucker was hired (F. 3, 5, R. 124–126). In addition, Army officials advised Acme that Tucker's father was suspected of "five-percenter" activities and that it was risky to hire Tucker; Joshua Epstein, Acme's president, ignored this advice (F. 8(d), 30, R. 128–129, 149). When Joshua Epstein ultimately came to suspect improper activities, he caused the resignation of the employees involved (F. 26–30, R. 147–149).[9]

Tucker, Norris and Jack Epstein were subsequently indicted for violation of the then Anti-Kickback Act, 60 Stat. 37 (F. 41, R. 149–150). After presentation of the government's case, the defendants' motion for acquittal was granted, on the ground that the Act—which at that time embraced only "cost-reimbursable" government contracts—did not apply to the Acme contract, a fixed-price contract with a provision for limited price redetermination. The district court stated that the defendants' conduct was "despicable and morally reprehensible, but unfortunately within the narrow letter of the law" (F. 54(j), R. 219–220).

Amendatory legislation was recommended by the Comptroller General (H. Rep. No. 1880, S. Rep. No. 1585, 86th Cong., 2d Sess.) and in 1960 the Act was amended to apply to all negotiated contracts including

[9] Jack Epstein's resignation, however, was delayed for nearly a year. During that time he replaced Norris as plant superintendent (F. 26, 29, R. 147–149). The Court of Claims found that the delayed resignation was "understandable in view of the relationship that existed" between Jack and Joshua Epstein (F. 30, R. 149).

contracts such as the one in this case (74 Stat. 740, 41 U.S.C. 51). This amendment was retroactive.[10]

2. PROCEEDINGS BELOW

In 1957, after failing to obtain an administrative settlement, Acme brought this action in the Court of Claims, alleging that the government's cancellation was a breach of contract and seeking "full restitution of its costs" or, alternatively, damages. Acme contended that the Army had used the statutory violations as an excuse to mask the real reason for cancellation—the fact that 75 mm. recoilless rifles had become obsolete (F. 47, R. 201). After full trial before a Commissioner, and extensive proceedings before the full court, the Court of Claims found that the obsolescence of the rifles and Acme's illegal activities were both reasons for cancellation and that either

[10] The original statute provided that the amount of any kickback, "whether heretofore or hereafter paid or incurred by the subcontractor," could not be charged under a subcontract and, if charged, was recoverable by the United States. 60 Stat. 37. The 1960 amendment, in extending the Act to all negotiated contracts, did not change this retroactive feature. 74 Stat. 740. The Comptroller General, in explaining his proposed amendment (which was enacted into law without material change), stated in a letter reprinted in the committee reports (H. Rep. No. 1880, *supra*, pp. 5–6; S. Rep. No. 1585, *supra*, p. 8):

> The proposed amendment does not disturb the retrospective feature of the act. It is not our intention, nor would it be practicable, for our Office to examine all contracts negotiated prior to the time the amendment may become law. However, in the event that current audits disclose kickback practices, the General Accounting Office should have the authority to take appropriate action with respect to violations under prior negotiated contracts

would have sufficed in the absence of the other (F. 50(a), R. 204–205). Moreover, the court found that the Army's decision to cancel for statutory violations, instead of invoking the contractual procedure for termination for convenience of the government, "was not controlled by considerations of termination costs, but rather by the Army's interest in promoting morality in public procurement" (F. 50(a), R. 204). The court therefore rejected Acme's contention that the government had acted in bad faith (R. 121–122).

a. The court found that Acme employees had accepted the kickbacks described above (F. 18–25, R. 139–147), but held that these activities did not justify cancellation of the contract. Hence, the government was liable for breach of contract for terminating the contract. The court reasoned that the Anti-Kickback Act provides for a specific civil remedy—recovery of the kickbacks—in addition to criminal sanctions, and that any further civil remedy is impliedly negatived. On this basis the court distinguished *United States* v. *Mississippi Valley Generating Co.*, 364 U.S. 520 (the *Dixon-Yates* case), where violation of a conflict-of-interest statute that provided only a criminal remedy was held to justify cancellation of a government contract. The court also concluded that the statutory violations here, unlike those in the *Dixon-Yates* case, were not related to the negotiation and execution of the prime contract and consequently did not taint the entire transaction. The court further distinguished *Dixon-Yates* on the ground that the conspirators here

had defrauded Acme as well as the government (R. 87–94).[11]

b. With regard to Acme's remedy, the Commissioner of the Court of Claims had rejected Acme's contention that it was entitled to full restitution of its costs, and had held that the proper remedy was to award Acme the damages actually suffered as a result of the government's breach, *i.e.*, to place Acme in the financial position it would have attained had the government not cancelled the contract (R. 50–56). The Commissioner found that Acme would have recouped a portion (albeit not the whole) of its loss on the contract had it been permitted to complete performance (R. 74–75). Accordingly, he ruled that Acme should recover its post-cancellation expenses ($11,597) plus the difference between its loss on the completed portion of the contract ($673,053) and the amount it would have lost on the entire contract had it not been cancelled ($550,409). He thus recommended an award to Acme (exclusive of awards to its subcontractors) of $134,241 (R. 76).

The Court of Claims reversed the Commissioner's ruling on damages (R. 105–111). It held that Acme was entitled to be returned to its *status quo* before the contract, and, therefore, to restitution of the value of the services it had rendered under the contract. The value of these services was to be measured, not by the contract price, but by Acme's actual costs (which were

[11] The Court also deemed it relevant that, although the 1960 amendment to the Anti-Kickback Act—which was concededly intended to apply to prior events—clearly covered these kickbacks, the application of the original Act to the government contract here involved was "highly questionable" (R. 92–93).

greatly in excess of the contract price), except to the extent that the government could show that these costs were excessive.[12] The effect of this ruling is that Acme, which would have lost $550,409 if the contract had been fully performed, is to be made whole except insofar as the government can demonstrate that Acme's costs were excessive; and the government, which agreed to buy the 75 mm. rifles at a cost not to exceed $384.95 each, is (subject to the same reservation) required to pay approximately $877.77 per rifle.

SUMMARY OF ARGUMENT

Respondent (Acme) entered into a negotiated contract with the government to manufacture recoilless rifles. The project was to be largely subcontracted. Key employees of Acme, however, had received bribes from firms awarded major subcontracts, in violation of the Anti-Kickback Act, and the government cancelled the contract believing it to be tainted by the violations. The Court of Claims held (1) that the government was not entitled to cancel the contract for that reason and hence was guilty of breach of contract, and (2) that Acme was entitled by way of remedy therefor to restitution of the reasonable costs it had expended in performing under the contract, even though these costs were greatly in excess of any return Acme could have earned had completion of its per-

[12] Excessiveness was to be determined primarily by comparing "Acme's costs with those of other manufacturers of the same rifles during that period, taking into consideration that Acme should be permitted greater reimbursement than established manufacturers because of its inexperience and the anticipated benefits of its entry as a competitor" (R. 110).

formance not been prevented by the government's cancellation. We challenge both rulings of the Court of Claims—that the government committed a breach and that the restitutionary relief decreed by the court was a permissible remedy for the breach in the circumstances of this case.

I

It is established that the government may, without fault or liability, cancel a contract on the ground that it is tainted by illegal conduct, if such a remedy, although not specified in the statute making the conduct illegal, is nevertheless consistent with, and essential to, attainment of the statutory goals. *United States* v. *Mississippi Valley Generating Co.*, 364 U.S. 520 (the *Dixon-Yates* case). The present case satisfies this standard.

The cardinal vice at which the criminal proscription of subcontractors' kickbacks is aimed is the selection of subcontractors on grounds other than competitive merit, with the attendant danger (a substantial one since major procurement contracts typically involve substantial subcontracting) that the performance of the contract will be less adequate and less expeditious, and the contract price higher, than it would have been if bribery had played no role in the award of the subcontracts. Correction is not assured by the criminal sanction in the Anti-Kickback Act or by the provision for recover of the amount of the kickbacks (the only remedies expressly provided in the Act). Neither restores to the public the monetary equivalent (if, indeed, that could be ascertained) of the injuries it may have suffered as the result of the selection of the sub-

contractors on a corrupt basis. Frequently, the only assured means of extirpating the continuing effects of the corruption will be to terminate the agreement.

We stress finally that the fundamental purpose of the anti-kickback statute, like the conflict-of-interest statute involved in *Dixon-Yates*, is a prophylactic one. The remedy we invoke is essential to effective policing and deterrence of kickbacks. They are normally secret, and the prime contractor is in an immeasurably better position than the government to detect and prevent derelictions by his agents—if he has an incentive to do so. Only the threat of cancellation is likely to provide that incentive.

II

Assuming that the government was guilty of a breach of contract, the restitutional remedy prescribed by the Court of Claims was not justified. Restitution as a remedy for breach of contract is essentially equitable in nature. Its purpose is to supplement the conventional damages remedy in instances where damages are inadequate and relief measured by the breaching party's gain is just and proper. These are principally cases where for obvious reasons prorating the contract price falsely or inadequately measures the injury suffered by the innocent party. But that is not the situation here.

In the first place, the contract was unquestionably a losing one from Acme's standpoint. To allow restitution of its costs of performance would give Acme a windfall far in excess of the actual injury it sustained because of the government's cancellation. This is a punitive result incompatible with the basic pur-

pose of contract remedies—to protect the bargain struck by the parties. Secondly, the government's breach was an innocent one, grounded in a good-faith belief that it was entitled to cancel the contract because of the kickback and other violations that it had discovered. This makes the case especially inappropriate for a punitive award. Thirdly, Acme should not be heard to complain of being held to its contract measure of damages. It entered into the contract in full awareness of the considerable risk it was taking that the contract would prove unprofitable. It also assented to a termination-for-convenience provision under which the government could have cancelled for reasons sufficient unto itself without being liable for anything more than the actual damages thereby caused.

The Court of Claims' award of restitutionary relief here also runs counter to important federal policies. It has never been the policy of Congress to permit punitive judgments to be levied against the government; yet that is the practical consequence of the holding below. It is also settled policy to avoid cost reimbursable procurement contracts, under which the government's obligation is measured by the contractor's costs rather than by a fixed price established in advance by competitive bidding or negotiation. Finally, to hold the government to an enhanced liability in cases like this one will inevitably tend to discourage vigorous implementation of the various statutes designed to assure probity on the part of government contractors.

ARGUMENT

I. WHERE RESPONSIBLE OFFICIALS OF A PRIME GOVERNMENT CONTRACTOR ACCEPT BRIBES FROM THE SUBCONTRACTORS IN VIOLATION OF THE ANTI-KICKBACK ACT, THE GOVERNMENT IS ENTITLED TO CANCEL.

A. THE RIGHT TO CANCEL A CONTRACT BECAUSE OF A STATUTORY VIOLATION IS PROPERLY IMPLIED WHEN THAT REMEDY IS NECESSARY AND APPROPRIATE TO EFFECTUATE THE STATUTORY POLICIES

The Anti-Kickback Act forbids a subcontractor to pay a fee or gratuity to an officer or employee of a government contractor as an inducement to award the subcontractor a subcontract. 41 U.S.C. 51. The unmistakable purpose of this prohibition is to protect the integrity of federal procurement, in which subcontracting plays a major role.

The key employees of Acme responsible for the contract in this case violated the Anti-Kickback Act by awarding subcontracts to subcontractors who had bribed them. While the Act imposes a criminal sanction for its violation, and also permits the government to sue to recover the amount of any illegal kickbacks, it does not expressly authorize the cancellation of a contract under which illegal kickbacks have been made. The question is whether that additional remedy, although not affirmatively declared by the statute, is nonetheless available.

Courts have frequently found additional remedies to be implicit in the scheme of federal statutes. *Frost & Co.* v. *Mines Corp.*, 312 U.S. 38, 43. Thus, private rights to damages or injunctive relief are commonly inferred from regulatory enactments. *E.g.*, *J. I. Case* v. *Borak*, 377 U.S. 426; *Tunstall* v. *Brother-*

hood of Locomotive Firemen & Enginemen, 323 U.S. 210; *Fairport P. & E. R. Co.* v. *Meredith*, 292 U.S. 589; *Texas & Pacific Ry.* v. *Rigsby*, 241 U.S. 33; *Brown* v. *Bullock*, 294 F. 2d 415 (C.A. 2); *Fitzgerald* v. *Pan American Airways, Inc.*, 229 F. 2d 499 (C.A. 2); *Reitmeister* v. *Reitmeister*, 162 F. 2d 691 (C.A. 2). Governmental injunctive remedies have likewise been inferred. *E.g.*, *Sanitary District* v. *United States*, 266 U.S. 405, 426; *United States* v. *Republic Steel Corp.*, 362 U.S. 482, 491–492. Cancellation of contracts tainted by illegal conduct is also a well recognized remedy allowable in appropriate cases though not expressly authorized by statute. *E.g.*, *United States* v. *Mississippi Valley Generating Co.*, 364 U.S. 520; *Mammoth Oil Co.* v. *United States*, 275 U.S. 13; *Pan American Co.* v. *United States*, 273 U.S. 456; *Crocker* v. *United States*, 240 U.S. 74; *Burck* v. *Taylor*, 152 U.S. 634; *Miller* v. *Ammon*, 145 U.S. 421; *Bank of the United States* v. *Owens*, 2 Pet. 527; *City of London Electric Lighting Co.* v. *London Corp.*, [1903] A.C. 434 (House of Lords); *McConnell* v. *Commonwealth Pictures Corp.*, 7 N.Y. 2d 465, 166 N.E. 2d 494; *Finch* v. *Riverside & A. Ry. Co.*, 87 Cal. 597, 25 Pac. 765; *Northport* v. *Northport Townsite Co.*, 27 Wash. 543, 68 Pac. 204; II Restatement of Contracts (1932), § 347; 6A Corbin, *Contracts* (1962 ed.), § 1373.

The leading recent case on contract cancellation as an implied remedy for violation of a federal statute is *United States* v. *Mississippi Valley Generating Co.*, *supra* (the *Dixon-Yates* case). The government contract in that instance had grown out of a proposal

resulting from negotiations in which the government's representative had at the same time been an officer of a company that expected to profit from the transaction. Having initially found that this individual had violated a federal conflict-of-interest statute (18 U.S.C. 434), the Court next addressed itself to the question whether cancellation was permissible as an implied remedy for the violation. The Court declared that the proper test was "whether the sanction of nonenforcement is consistent with and essential to effectuating the public policy embodied in" the statute and "that a contract is not to be enforced when it arises out of circumstances that would lead enforcement to offend the essential purpose of the enactment" (364 U.S. at 563). Finding that the "primary purpose" of the conflict-of-interest statute was "to protect the public from the corrupting influences that might be brought to bear upon government agents who are financially interested in the business transactions which they are conducting on behalf of the Government" (364 U.S. at 563), it concluded (*ibid.*): "This protection can be fully accorded only if contracts which are tainted by a conflict of interest on the part of a government agent may be disaffirmed by the Government. * * * Were we to decree the enforcement of such a contract, we would be affirmatively sanctioning the type of infected bargain which the statute outlaws and we would be depriving the public of the protection which Congress has conferred."

The Court deemed irrelevant the fact that the contractor itself may not have known of, or been respon-

sible for, the illegal conduct. "Although nonenforcement frequently has the effect of punishing one who has broken the law, its primary purpose is to guarantee the integrity of the federal contracting process and to protect the public from the corruption which might lie undetectable beneath the surface of a contract conceived in a tainted transaction. [Citation omitted.] It is this inherent difficulty in detecting corruption which requires that contracts made in violation of Section 434 be held unenforceable, even though the party seeking enforcement ostensibly appears entirely innocent." 364 U.S. at 564–565.

We believe these precepts are applicable in the present case as well.

B. THE TEST OF THE *DIXON-YATES* CASE IS MET HERE; PROTECTION OF THE INTEGRITY OF THE PROCUREMENT PROCESS REQUIRES THAT A CONTRACT TAINTED BY KICKBACK VIOLATIONS, LIKE ONE TAINTED BY A FORBIDDEN CONFLICT OF INTEREST, BE PROMPTLY TERMINATED WITHOUT LIABILITY TO THE GOVERNMENT

The *Dixon-Yates* decision lays down a simple and pragmatic test: the government may, without fault, cancel a procurement contract if such a step is necessary to effectuate the policies of the statute that has been violated. Applying that test here, we believe the government was entitled to cancel the Acme contract.

1. Congress recognized that, in view of the extent to which subcontracting is typically involved in the performance of government contracts,[13] bribes taken

[13] The Comptroller General's report to Congress, in recommending the 1960 amendment that broadened the coverage of the Act, pointed to the "enormous extent of subcontracting" involved in weapons contracts. H. Rep. No. 1880, 86th Cong., 2d Sess., p. 5. The Acme contract in issue here was largely subcontracted. See Statement, *supra*, pp. 4–5.

by purchasing officers of contractors in connection with the award of subcontracts undermine government procurement in essentially the same manner, and to a comparable degree, as bribes taken by the government's own purchasing officers. Accordingly, although the primary purpose of the anti-kickback bill originally proposed by the Comptroller General had been to provide a secure legal basis for recovering kickback payments discovered on audit,[14] Congress added to the bill a severe criminal penalty modeled upon that applicable to the bribery of government contracting officers.[15]

The analogy to bribery of government procurement officers is instructive with respect to the basic concerns that led Congress to attempt to prevent and punish kickbacks from subcontractors to prime government contractors. In both instances, there is substantial danger that the bribes or kickbacks will ultimately be paid by the government in the form of a higher contract price. But there is a greater danger—that

[14] H. Rep. No. 212, 79th Cong., 1st Sess., pp. 4–6 (report of Comptroller General, October 5, 1943).

[15] The penalty prescribed by the Act—a fine of $10,000 or two years imprisonment or both—is identical to the penalty prescribed in 1946 (when the Act was passed) for bribing a government employee to procure a government contract. 18 U.S.C. 202 (1946 ed.). The War Department witness who first suggested a criminal penalty at the congressional hearings stated that the statute regarding bribery of government contracting officers had been used as a model in drafting the suggested penalty. Hearings on H.R. 131 before House Committee on Expenditures in the Executive Departments, 79th Cong., 1st Sess., pp. 24, 25. The bill proposed by the Comptroller General contained no criminal penalty. *Id.*, pp. 1–2.

the contract, if it was conceived in corrupt dealings, will ill serve the government's needs.

The public interest in assuring that government contracts be awarded on the basis of merit need not be labored. The interest in assuring that prime government contractors award subcontracts on a merit basis stands on the same footing. Often, as here, the project contemplated by government procurement contract is largely subcontracted. If prompt, efficient, and economical performance of the contract is to be assured, it is essential that the subcontractors, no less than the prime contractor, be fully reliable. The feasibility of the contract, the likelihood that it can be completed for the contract price without upward redetermination, and even the amount that the prime contractor is willing to bid—all may depend upon his subcontracting arrangements. In recognition of their importance to the success of the contract, subcontractors are typically brought into the negotiations for the prime contract, and the government carefully reviews the prime contractor's subcontracting arrangements. Thus, in the present case the price of one of the subcontracts procured through a kickback represented almost one-third of the total price of the prime contract, and this subcontractor participated in the negotiation of the prime contract—as his stake in the total project warranted. (Statement, *supra,* pp. 4–5).[16]

[16] In light of the detailed finding of the Court of Claims on this point, its conclusion that the kickbacks "were in no way related to the negotiation and execution of [the prime contract]" (R. 94) appears unfounded.

A subcontractor who owes his subcontract to a kickback cannot be considered fully reliable. In selecting him, the prime contractor may have passed over far more competent firms. In addition, the price of the subcontract—and hence of the prime contract as well—may be inflated, and not merely by the amount of the kickbacks. A subcontractor who expects to obtain a subcontract by bribery has little incentive to stint in his estimates of cost and profit. The ordinary constraints of competition are absent where orders are awarded not on the basis of price and quality but because of kickbacks to officials of the prime contractor.

2. If we have correctly identified the principal evils of kickbacks from subcontractors to employees of prime government contractors, there can be little doubt that a government right of cancellation is a necessary adjunct to the remedies expressly prescribed by the Anti-Kickback Act, and one that should be recognized as implied in the Act. The express remedies are of themselves inadequate to provide an assured cure for the principal injurious consequences of kickbacks. The criminal sanction doubtless deters many from violating the statute; but in cases where, despite the criminal penalty, a bribe is given, punishment of the guilty persons leaves the ill effects of their illegal conduct intact. Those effects live on in the contract. If the government is bound to the contract, it has no remedy against either the unreliability of the subcontractors' performance or the possible inflation of the contract price incident to the method of letting the subcontracts.

The civil remedy provided by the Act—recovery of the kickbacks—is likewise incomplete. The price of the subcontract (reflected in the contract price) may well be greater, and the performance of the subcontractor less satisfactory, if the subcontract was awarded on the basis of bribery rather than competitive merit; and the result may be to increase substantially the real cost of the contract to the government. The full amount of the additional cost cannot, however, be recovered in a suit limited to the amount of the kickbacks.[17] Nor would a suit (assuming it were possible or feasible) against the corrupt individuals to recover damages for the injuries they caused the government be likely to provide complete relief, for those injuries are rarely measurable.[18] Additional remedies are thus necessary. Cancellation of the contract—which frees the government from further ob-

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[17] The inadequacy of the civil remedy prescribed in the Act provides a complete answer, we think, to the view of the Court of Claims (R. 93–94) that a different result is warranted in this case from that in the *Dixon-Yates* case because the Anti-Kickback Act contains a civil as well as criminal sanction. Moreover, the legislative history contains no suggestion that the provision for recovery of the kickbacks was to be exclusive of all other civil remedies. Congress merely wished to assure that the right to such recovery would be available in addition to the remedies ordinarily recoverable against corrupt practices. H. Rep. No. 212, 79th Cong., 1st Sess., pp. 2, 5. Cancellation, as we have seen (p. 18, *supra*), is such a remedy.

[18] See *Aberdeen Railroad Company* v. *Blaikie Bros.*, 1 MacQueen's Appeal Cases, 461, 472, quoted in *United States* v. *Carter*, 217 U.S. 286, 306–307: "It obviously is, or may be, impossible to demonstrate how far in any particular case the terms of such a contract [a contract involving an agent's conflict of interest] have been the best for the interest of the *cestui que trust*, which it was possible to obtain."

ligation under a contract whose terms may well be prejudicial to the public interest because of the kickback violations—will in many cases be the only adequate one.[19]

The case is similar to *Dixon-Yates.* Because the government's representative in the *Dixon-Yates* contract negotiations was guilty of a conflict of interest, there could be no assurance that the contract was in the public interest. Punishing the guilty person, or even recovering (had that been possible) the value of any benefit received by him, would not have protected the government if the contract was indeed tainted by the conflict of interest. Here, too, there is a conflict of interest.[20] The prime contractor's key employees, in awarding subcontracts, were hardly guided by the interest of the contracting parties; their self-interest

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[19] It is no answer that in such cases the government should persuade the prime contractor to cancel the tainted subcontracts. Its efforts at persuasion may in many cases be wholly unavailing. It will frequently be prohibitively expensive for a contractor to change major subcontractors in midstream, so that his only practical course will be to let the tainted subcontracts stand—with the incidental consequence of providing profit to the subcontractors who committed commercial bribery in order to obtain the government's business. In this case, indeed, Acme—after discovery of the kickbacks—specifically agreed not to assert any defense of illegality against the claims of the principal subcontractor, All Metals, which had made a kickback (F. 64, R. 236–237).

[20] The illegality here is actually more flagrant than in *Dixon-Yates.* There the corruption was merely potential; the government negotiator had an interest in a potential subcontractor, but no actual corruption of judgment on his part was shown. Here bribes were actually solicited and received, and subcontracts were awarded to companies giving the bribes.

was served by eliciting graft from compliant subcontractors. Subcontracting being so dominant a characteristic of the contract, the result of this corruption of judgment was a contract whose performance from the government's standpoint is highly suspect.[21] The consequences of the corruption are not expunged merely by criminal punishment or civil recovery of the kickbacks and may indeed be impossible to measure. Cancellation of the contract is required to protect the public interest from any further injury under a contract negotiated in circumstances which raise a grave doubt whether it is consistent with the public interest.

3. An additional reason for allowing cancellation is the "inherent difficulty in detecting corruption." *United States* v. *Mississippi Valley Generating Co.*, 364 U.S. 520, 565. Normally, of course, kickbacks are concealed. Detection is difficult. And the government is not well situated to determine whether employees of its contractors are taking bribes from subcontractors. Unless the contractor himself is vigilant in policing his employees and subcontractors, the statute is likely to be widely disobeyed. But without the threat of cancellation the contractor may have little incentive to root out kickbacks. He may indeed condone the practice, expecting to pass on to the government any additional costs he may incur.

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[21] To be sure, the contract turned out to be a losing one for Acme. But that may prove no more than that Acme's costs were higher than anticipated—a circumstance which may be related to the selection of principal subcontractors on a corrupt basis.

The facts of the present case illustrate the importance of obtaining the contractor's active co-operation—through threat of cancellation—if there is to be an effective program of preventing kickbacks. Acme's officers (other than the conspirators) were found to have had no conscious knowledge of the kickbacks. However, had they thought the government would be entitled to cancel if it discovered kickbacks, and so been on their guard, they would doubtless have discovered them. Suspicious circumstances abounded (see Statement, *supra*, pp. 8–9).

The Court of Claims' suggestion that Acme should be exonerated from responsibility for the illegal kickback activities of its high-ranking executives on the ground that the executives intended to defraud Acme[22] (R. 88–89, n. 12) is thus wide of the mark. Kickbacks were taken by the general manager of Acme's chief plant (who was also the son of Acme's president and principal stockholder and a stockholder in his own right) and by the Acme officials in charge

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[22] The Court of Claims' assumption that the aim of Tucker, Norris, and Epstein was to defraud Acme rather than the government is apparently based on the fact that Acme's costs were so far in excess of the maximum contract price that it would have been impossible to pass the kickback charges on to the government through price redetermination, even if the conspiracy had not been discovered. However, the kickback arrangements in this case were all made either before the prime contract was executed or within a few weeks thereafter (F. 18–25, R. 139–147), and at that time, surely, Acme did not realize it had a losing contract, else it presumably would not have signed it. And had it not been a losing contract, undiscovered kickbacks could have been passed on to the government through price redetermination—in which event Acme would not have been injured.

of operations, sales and government contracts (F. 16, 20, R. 138, 141). Having chosen these officials to conduct its government contract business, Acme may properly be held responsible for their actions in regard to that business even if designed to benefit themselves rather than Acme.[23] Any other rule would undermine the contractor's incentive to take steps to ensure the integrity of its employees.

In short, the root error of the decision below is its failure to recognize that the fundamental purpose of the anti-kickback statute, no less than the conflict-of-interest statute involved in *Dixon-Yates,* is a prophylactic one.[24]

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[23] Cf. *Gleason* v. *Seaboard Ry.*, 278 U.S. 349, 357, where this Court held a railroad liable for its employee's issuance of a false bill of lading, ruling that "the agent's secret purpose to benefit himself by his breach of duty" was not ground for refusing to apply the principles of *respondent superior.* See, also, *Standard Surety & Gas Co.* v. *Plantsville Nat. Bank*, 158 F. 2d 422, 424–425 (C.A. 2), certiorari denied, 331 U.S. 812.

[24] We note briefly the Court of Claims' observation that it is "highly questionable" whether the kickbacks—which covered the period 1952–1954—violated the Anti-Kickback Act as originally enacted in 1946, since that Act applied only to "cost reimbursable" contracts, and the contract here was a fixed-price contract with a price redetermination clause (R. 93). It is clear that these kickbacks violated the Anti-Kickback Act as amended in 1960, and that the amendment was retroactive (see Statement, *supra*, p. 10, n. 10). We thus fail to see the relevance of the court's observation. In addition, we point out that the only appellate ruling on the question held the original 1946 Act applicable to price redetermination contracts. The 1946 Act applied where the prime contract was "on a cost-plus-a-fixed fee or other cost reimbursable basis." 60 Stat. 37. *United States* v. *Barnard*, 255 F. 2d 583, 588 (C.A. 10), certiorari denied, 358 U.S. 919, held the 1946 Act applicable to a price redetermination contract, as an "other reimbursable basis contract." To be sure, as the Court of Claims pointed out (R. 93), in *Barnard* the

II. TO ALLOW RESTITUTION IN THE CIRCUMSTANCES OF THE PRESENT CASE—WHERE DAMAGES WOULD FULLY COMPENSATE THE PLAINTIFF FOR THE LOSS HE SUSTAINED AS A RESULT OF THE ALLEGED BREACH—WOULD OFFEND SOUND PRINCIPLES OF CONTRACT LAW AND IMPORTANT FEDERAL POLICIES GOVERNING PROCUREMENT CONTRACTS

If we are correct in Point I—that the government acted within its prerogatives in cancelling the contract with Acme—no question of remedy remains. In this part we assume that there was a breach and address ourselves to the question of the proper remedy.

Tenth Circuit emphasized that the prime contract contained no limitation on the range of price revision. However, this fact was not crucial to the Tenth Circuit's holding. The court reasoned (255 F. 2d at 588):

> [The contract] partook of both aspects. It was in substance and effect a fixed price and "other reimbursable basis contract". And partaking in part of an "other reimbursable basis contract", it came within the range of [the Act].

Similarly, Acme's contract—despite the ceiling on price redetermination—"partook of both aspects." Moreover, the reason for the limitation in the 1946 Act to cost-reimbursable contracts is that, under such contracts, kickbacks may be charged through to the government. In the present case, at the time the kickback conspiracy was formed, the individuals involved had every reason to expect that the kickback would be charged through to the government (see n. 22, *supra*).

Moreover, the kickbacks were undoubtedly in violation of State law, regardless of the nature of the prime contract. The kickbacks took place primarily in Pennsylvania, with some events occurring in New Jersey and New York. All three States have statutes prohibiting commercial bribery of this kind. 18 Pa. Stat. Ann. (Purdon's), § 4667; New York Penal Law (McKinney's), § 439; 2A N.J. Stats. Ann., § 170–88. And there can be no doubt that the kickbacks violated "obvious ethical or moral standards." *Muschany* v. *United States*, 324 U.S. 49, 66–67.

Under conventional principles of contract law, the successful plaintiff in an action for breach of contract will, in many cases, be permitted to elect among remedies. He may ask for specific performance of the terms of the contract (a remedy not in issue here).[25] Alternatively he may ask for damages—that is, to be placed in the same position he would have occupied had the contract been fully performed—and thereby recover the profit he would have made but for the breach. Assuming that the government breached the contract here, we grant that Acme is entitled to damages, for the evidence shows that, had the contract been fully performed, Acme would have recouped about 20 percent of the heavy losses it sustained on the rifles it delivered prior to the breach (see Statement, *supra*, p. 12).

There is a third remedy frequently available, at least where, as in the present case, the breach prevented the other party from completing his performance under the contract—that of restitution.[26] The measure of restitutionary relief is the value of the partial performance. The theory is that the victim of a breach has a claim to be placed, if he chooses, in the position he occupied before the contract was

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[25] A government contractor is normally not entitled to such relief, owing to the standard provisions of government contracts and the limitations on the jurisdiction of the courts in contract suits against the United States. See 28 U.S.C. 1346 (a) (2), 1491.

[26] We deal here with restitution as a remedy for breach of contract. It is, of course, frequently granted in cases of "quasi-contract"—as where benefits have been received by mistake or under a contract that cannot be enforced because it violates the Statute of Frauds.

made, as distinguished from the position he would have attained had the contract been fully performed. *E.g.*, II Restatement of Contracts (1932), § 347, *Comment b;* 5 Corbin, *Contracts* (1964 ed.), § 1102, p. 548; § 1107, p. 573. Hence, if, by performing his obligation under the contract until prevented from continuing by the breach of the other party, the victim conferred a benefit upon the other, he may demand that the monetary equivalent of that benefit be restored to him.

Applying this reasoning, the Court of Claims held that Acme should be awarded the value of Acme's services less the payments already made. The court also ruled that the value of the services was to be measured by the costs (unless shown to be excessive) incurred by Acme. These costs far exceeded both the contract rate and Acme's damages. Under this ruling Acme stands to recover an amount far larger than its actual damages or even the total price of the uncompleted portion of the contract.

We believe that the Court of Claims' grant of restitutionary relief contravenes sound principles of general contract law and important federal procurement policies. This is not to suggest that restitution is never available as a contract remedy in suits under the Tucker Act. We urge no such principle. See, *e.g., New York Mail & Transp. Co.* v. *United States,* 154 F. Supp. 271 (Ct. Cl.), certiorari denied, 355 U.S. 904. On the other hand, we think the remedy should not be applied where the damages remedy is adequate to compensate the plaintiff for all the loss he has suffered as a result of the breach, and

where restitution would place the plaintiff in a better position than he would have attained had the contract been completed.

A. RESTITUTION IS DESIGNED TO PROVIDE A FLEXIBLE, ESSENTIALLY EQUITABLE, REMEDY IN SITUATIONS WHERE DAMAGES ARE NOT SO ACCURATE A MEASURE OF THE INJURY CAUSED BY THE BREACH AS IS THE VALUE OF THE SERVICES RENDERED UNDER THE CONTRACT TO THE DEFENDANT

The traditional common law remedy for breach of contract was damages. In some respects, however, it was a rather rigid remedy that was inadequate to do justice in all situations. Restitution, like specific performance and other equitable remedies, arose in response to the need for greater remedial flexibility. See *Nash* v. *Towne,* 5 Wall. 689; *Moses* v. *MacFerlan,* 2 Burr. 1005 (Lord Mansfield); 5 Corbin, *supra,* § 1103. An example will illustrate the kind of problem that restitution (as a remedy for breach of contract, see note 26, *supra*) was designed to meet.

Suppose *A* employs *B* as his valet for one year, under a contract which provides that *B* shall receive $5,000 at the end of the year. After six months *A* wrongfully discharges *B,* who promptly takes another job as a valet at the same salary. If *B* sues *A* for damages, he can presumably recover only $2,500—the contract price less what he earned doing the same work for someone else for the balance of the contract period. Suppose, however, that the fair value of the service rendered *B* to *A* during the six months before the wrongful discharge was $3,000. Should *B* be permitted to sue, not for the contract price, but for restitution of the value of the service rendered—$3,000? The answer is yes. *B* bargained for a year's

employment—not six months. He was willing to work for $5,000 for one year but may well not have been willing to work for half that amount for six months. To give him merely a prorated share of the contract price—the practical result of awarding him damages—is thus to give him less than he bargained for. See II Restatement of Contracts, § 347, *Illustration* 2, p. 589.

Or suppose a building contractor begins a project but, before he can complete it, the owner wrongfully terminates the contract. To award the contractor only a prorated share of the contract price would ignore the possibility that, had he been allowed to complete the project and so earn the entire contract price, he might have made a greater profit by reducing his costs in the later stages of his performance. See *Rodemer* v. *Hazlehurst & Co.*, 9 Gill. 288 (Md.); *Adams* v. *Healy*, 227 Mich. 159, 198 N.W. 584; *Derby* v. *Johnson*, 21 Vt. 17.

In both types of situation (and we note that employment and building contracts appear to be the types most frequently involved in contract restitution cases) the traditional remedy is not adapted to measuring accurately the extent of the loss suffered by the innocent party as the result of the breach. In both situations, moreover, the plaintiff has rendered the defendant valuable services in performing his obligation under the contract until prevented from continuing by the latter's wrongful action. It is fair and just that the defendant be required to restore to the plaintiff the value of the services rendered, rather

than that the plaintiff be remitted to a damages remedy that is likely to be inadequate to redress the injury caused by the breach. See Patterson, *Builder's Measure of Recovery for Breach of Contract*, 31 Col. L. Rev. 1286, 1302.

We view restitution, then, as a supplement to the conventional damages remedy, flexible and essentially equitable in its nature and purposes, and appropriately invoked where damages are inadequate to compensate the aggrieved party for the loss of his bargain.[27] See Fuller and Perdue, *The Reliance Interest in Contract Damages*, 46 Yale L.J. 52, 75–80; Palmer, *The Contract Price as a Limitation on Restitution for Defendant's Breach*, 20 Ohio St. L. J. 264, 278–279. Thus viewed, the availability of restitution cannot be reduced to a hard-and-fast rule applicable in all circumstances. We accordingly suggest no such rule. We are content to show that the policy and rationale of restitutionary relief, as we conceive it, do not support permitting the plaintiff to recover his costs of performance where damages are completely adequate to compensate him for the loss resulting from termination of the contract and restoration of his costs

[27] That inadequacy of the damages remedy is the true rationale of restitutionary relief is indicated by the fact that, when the innocent party has completed performance prior to the breach, he cannot ask restitution, but is limited to damages based upon the contract price. II Restatement of Contracts, § 350. For it is only where performance has been interrupted due to the breach that the problem of prorating the contract price—a solution likely to be inadequate to measure the full extent of the innocent party's loss—arises.

would give him a pure windfall. That, as we show, is the case here.

A caveat is necessary. We do not claim that the concept of restitutionary relief advanced herein would commend itself to every State court. Some might allow restitution in the circumstances of this case,[28] while others probably would not.[29] In adapting the law of restitution to actions upon government contracts under the Tucker Act, this Court is not, of course, bound by the views of particular States. We urge the Court to hold that the essence of restitutionary relief, soundly conceived, is recognition that the normal remedy for breach of contract is to give the innocent party the value of the bargain he struck

[28] See *Philadelphia* v. *Tripple*, 230 Pa. 480, 79 Atl. 703; *Johnston* v. *Star Bucket Pump Co.*, 274 Mo. 414, 202 S.W. 1143; *Connolly* v. *Sullivan*, 173 Mass. 1, 53 N.E. 143; *Valente* v. *Weinberg*, 80 Conn. 134, 67 Atl. 369; *Boomer* v. *Muir*, 24 P. 2d 570 (Cal. App.); *Southern Painting Company of Tenn.* v. *United States*, 222 F. 2d 431 (C.A. 10); *Heitz* v. *Sayers*, 32 Del. 207, 121 Atl. 225; *Matter of Montgomery*, 272 N.Y. 323, 6 N.E. 2d 40; *Stark* v. *Magnuson*, 212 Minn. 167, 2 N.W. 2d 814; *Pelletier* v. *Masse*, 49 R.I. 408, 143 Atl. 609; *Peist* v. *Richmond*, 97 Vt. 97, 100, 122 Atl. 420, 421; *Thompson* v. *Gaffey*, 52 Neb. 317, 72 N.W. 314; *Rustles* v. *Christensen*, 207 Wis. 326, 241 N.W. 635.

[29] See *Oakley* v. *Duluth Superior Dredging Co.*, 223 Mich. 478, 194 N.W. 123; *Reynolds* v. *Levi*, 122 Mich. 115, 80 N.W. 999; *Kehoe* v. *Rutherford*, 56 N.J.L. 23, 27 Atl. 912; *Kitchell* v. *Crossley*, 90 N.J.L. 574, 101 At. 179; *Farnum* v. *Kennebec Water District*, 170 Fed. 173 (C.A. 1) (applying law of Maine); *Keeler* v. *Clifford*, 165 Ill. 544, 46 N.E. 248; *Cleveland C., C. & St. L. Ry. Co.* v. *Moore*, 170 Ind. 328, 341–343, 82 N.E. 52, 56–57; *Wuchter* v. *Fitzgerald*, 83 Ore. 672, 163 Pac. 819; *Bailey* v. *Furleigh*, 121 Wash. 207, 208 Pac. 1091; *Noyes* v. *Pugin*, 2 Wash. 653, 27 Pac. 548; *Wellston Coal Co* v. *Franklin Paper Co.*, 57 Ohio St. 182, 48 N.E. 888; *Dickson* v. *Emmerson*, 154 Ore. 558, 562, 61 P. 2d 439, 441.

and no more, and that a different measure of relief is appropriate only where the traditional remedy is inadequate for this purpose.

B. MEASURED BY SOUND PRINCIPLES OF RESTITUTIONARY RELIEF, THE CONTRACTOR IS NOT ENTITLED TO A RECOVERY IN EXCESS OF THE DAMAGES HE ACTUALLY SUFFERED AS A RESULT OF THE TERMINATION WHERE, AS HERE, THERE IS NO QUESTION OF THE ADEQUACY OF THE DAMAGES REMEDY

We think the circumstances of this case are such that to allow restitutionary relief as decreed by the Court of Claims would distort the policy and rationale of the restitution remedy under general contract principles. The cardinal circumstances are as follows.

1. In retrospect, it is indisputably clear that Acme entered into an unprofitable contract. Even had it been permitted to complete performance, it would have made no profit, albeit it would have reduced its losses. There is no ambiguity on this point. The record indicates clearly what Acme lost on the rifles it delivered to the government and what it would have earned on the remaining rifles. Plainly, it could not have recouped its earlier losses over the remaining life of the contract. Assuming—as we do throughout this part of our argument—that the government breached the contract in cancelling for statutory violations, we agree that Acme is entitled to recover the net sums it would have received on the remaining rifles, *i.e.*, those it was unable to deliver because of the government's termination. But we see no justification for awarding Acme the much larger sum representing its costs of producing the rifles that it did deliver under the contract—even assuming that

those costs were not excessive and that they may fairly be equated with the value received by the government from Acme's partial performance.

There can be no contention, in this case, that the contractor's remedy in damages would not adequately measure the loss it suffered as a result of the breach. We do not urge that damages here be measured simply by prorating the contract price, ignoring the consideration that declining costs over the life of the contract would have enhanced its profitability to the contractor. Precisely such a computation of declining costs was made; it formed the basis of the Commissioner's award of damages, which we believe provided the appropriate and complete relief for the injury caused by the breach. Nor is this a case where it can be cogently argued that limiting the plaintiff to the contract price gives him less than he bargained for. The contract price was computed according to the unit of production. It was simply the product of multiplying the number of rifles by the price of each individual rifle. To be sure, had fewer units been specified in the contract, Acme might have made a higher bid in recognition that its initial production costs were likely to be disproportionately high. But, to repeat, the Commissioner took full account of this factor in awarding Acme damages representing the sums it would have recouped on subsequent deliveries.

Finally, this is not a case where it is unfair to subject the plaintiff to the burden of proving his future costs as a basis for damages recovery. The contract contemplated that the contractor would be able to furnish reliable estimates of future costs in connection with price determination (R. 254–255). Acme's own ac-

countants accordingly were able to furnish detailed estimates (R. 206)—which were largely accepted by the Commissioner.

Since the damages awarded by the Commissioner would place Acme in the position it would have attained had no breach occurred, there is no justification for awarding Acme the greatly enhanced sum representing the costs it incurred in producing the rifles delivered under the contract. Such an award would give Acme a pure windfall. It would go much further than to repair the injury suffered by Acme as a result of the cancellation of the contract; it would repair the mistake Acme made when it entered into a losing contract. The short of it is that Acme incurred costs far in excess of the contract price not because the government cancelled the contract, but because of its own managerial mistakes and entrepreneurial fortunes. In these circumstances, restitution of costs cannot realistically be regarded as a remedy for the breach; it is punishment meted out to the breaching party. To punish for breach of contract cuts deeply against the grain of traditional contract principles.[20] We submit it is not a proper office for restitution or any other remedy for breach of contract.

It is no answer that, the government having breached, the contract must be treated as rescinded and adjustment made irrespective of its terms. The contract is the very basis of the restitution action; without the breach of the contract, there would be no

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[20] Under settled principles of contract law, the parties to a contract cannot prescribe penalties for its breach. *E.g.*, 5 Corbin, *supra*, §§ 1054, *et seq.*

cause of action. Furthermore, if restitution here is not viewed as a remedy upon the contract, but as a remedy sounding in quasi-contract or *quantum meruit*, no recovery is possible against the government under the Tucker Act, 28 U.S.C. 1491; *United States* v. *Minnesota Mutual Inv. Co.*, 271 U.S. 212, 717; *Merritt* v. *United States*, 267 U.S. 338; *Sutton* v. *United States*, 256 U.S. 575, 581.

Nor is it an answer that the government, having received a benefit from Acme, should be required to pay for it according to Acme's costs. The value to the government was not the cost to Acme, even assuming that cost was a fair one, but the contract price. There is nothing to indicate that the government would voluntarily have paid Acme two or three times the contract price for these rifles, albeit it desired to encourage entry of new competitors into the military-supply field. It might well have concluded that such an investment would be unwarranted, and that the money could be spent to greater advantage on other weapons. Or it might have decided to procure the rifles from other contractors—as it could have done at prices only slightly higher than the maximum contract price in the Acme contract.[21] There is, in sum, no basis for the view that the government was unjustly enriched because Acme spent

[21] The ceiling price of the contract with Acme was $384.95 per rifle (F. 7, R. 126). The government had received a bid of $452.60 from another contractor who was successfully producing rifles, and bids from other firms at $423, $484 and $684 respectively (F. 7, R. 126–127).

more than it anticipated in the production of these rifles."[32]

2. Even if, contrary to our suggestion, a punitive measure of damages for breach of contract may in some circumstances be warranted, surely it is not in a case like this, where the breach was neither wanton nor deserving of censure. The Court of Claims found that the government believed in good faith that the statutory and contractual violations of Acme and its employees warranted cancellation. If the government erred in that conclusion, the error was an innocent one. Certainly the government was the less culpable party in the course of events that led to the cancellation of the contract: The precipitating cause of the cancellation was the unethical and illegal conduct of key Acme employees. In view of the basically equitable nature of the restitution remedy, we think it important to stress the actual balance of equities in this case—and the highly technical sense in which the government, because it cancelled the contract, may be said to have acted wrongfully.

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[32] Compare *L. Albert & Son* v. *Armstrong Rubber Co.*, 178 F. 2d 182 (C.A. 2) (L. Hand, J.), which held that a seller of machinery who had breached by delaying delivery could deduct the buyer's loss on the contract from its recovery for expenses in preparing his factory for receiving the machines (which were never delivered). Under this well settled rule, if the plaintiff's expenses confer no benefit on the defendant, the plaintiff is not entitled to recovery in excess of his actual damages. It seems anomalous that if, as here, the plaintiff's expenses confer *some* benefit, he is entitled to recover his entire expenses though they are grossly disproportionate to the value of the benefit conferred. Hence, even if this Court concludes that the doctrine of restitution is applicable here, we urge it to reject the *measure* of restitutionary relief (costs) applied by the Court of Claims.

In this connection, we point out that Acme entered into this contract with full awareness of the risks involved. Indeed, the government had offered it a chance to withdraw its bid—which was so low as to raise doubts concerning Acme's ability to perform without loss—but Acme had declined, its eagerness to become a military supplier impelling it to enter upon a contract it knew to be risky. We also note that the contract contained a price redetermination clause, under which Acme might obtain payment above the contract price if its costs proved to be higher than anticipated; and most pointedly, that the contract contained a provision authorizing the government to terminate the contract "whenever the Contracting Officer shall determine that such termination is in the best interests of the Government." (R. 247.)

Had the government invoked this clause in cancelling the contract—as it was entitled to do on any ground—its maximum liability to Acme in termination costs would not have exceeded the amount adjudged by the Commissioner to be Acme's damages for breach of contract. (Compare F. 48, R. 202, with Commissioner's finding 84, R. 76.) Acme had in effect agreed that the government could at any time cancel the contract for reasons sufficient unto itself without being liable for any more than the actual damages caused by the cancellation. The government, to be sure, did not invoke this clause, believing that it was entitled to cancel the contract because of statutory violations without any liability. But, in view of its initial assent to inclusion of the termination-for-convenience provision, Acme has no equity in

CONCLUSION

For the foregoing reasons, we respectfully submit that the judgment below should be reversed.

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AUGUST 1966

U.S. GOVERNMENT PRINTING OFFICE: 1966

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claiming a larger judgment than that clause allows for a government cancellation without cause—merely because the government reasonably and in good faith believed that it *had* cause.

C. IMPORTANT FEDERAL POLICIES WOULD BE IMPAIRED BY ALLOWING RESTITUTION IN THIS CASE

Even if, as a matter of sound general contract principles, restitution is allowable in a case like this, we think it should be disallowed on policy grounds arising from the nature of government procurement contracts.

1. As noted in the preceding discussion, the Court of Claims would give Acme an award that is clearly punitive, in that it is grossly disproportionate to the actual injury sustained by Acme as a result of the government's breach. (That injury was the much smaller amount representing the sums Acme would have recaptured on the undelivered rifles.) Such an award of punitive damages contravenes the basic principles of contract remedies, but it is particularly anomalous where the defendant is the government. It is unsound to suppose that, by subjecting the government to suit for breach of contract, Congress in the Tucker Act intended to open the government to punitive judgments. In the context of suits against the government, the remedy accorded by the court below is unprecedented (see R. 106).[22]

[22] Compare 28 U.S.C. 2647 (Tort Claims Act); *Massachusetts Bonding & Ins. Co.* v. *United States*, 352 U.S. 128. See, also, *Missouri Pac. R.R. Co.* v. *Ault*, 256 U.S. 554, 563-565, holding that a statute subjecting the government, as owner and operator of the nation's railroads during World War I, to "all laws and liabilities as common carriers," did not authorize recovery

2. Where, as in the present case, restitution is applied so as to yield damages far in excess of those possible under conventional remedies for breach of contract, it becomes fictional to speak of the action as one upon the contract. The breach, to be sure, is the trigger that allows the restitution remedy to be invoked, but the remedy itself is independent of (if not contrary to) the terms of the contract. In such a case, the action realistically is one sounding in quasi-contract or *quantum meruit*—an action for the value of goods received without reference to a legal contract. The Tucker Act does not authorize such actions (see p. 39, *supra*).

3. The rule of damages applied by the Court of Claims has the effect of giving the contractor an option, in the event of the government's breach, of placing his contract on a full cost reimbursable basis. This new rule violates established federal procurement policies and regulations, which require government supplies and services to be purchased so far as possible on a fixed-price basis.[34] The federal policy in favor of fixed-price contracts is also expressed in

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of a civil penalty. "The purpose for which the Government permitted itself to be sued was compensation, not punishment." 256 U.S. at 564.

[34] The present regulation states: "whenever a reasonable basis for firm pricing exists * * *, the firm fixed-price contract shall be used, because its use under these circumstances will provide the contractor with a maximum profit incentive to control the costs of performance." 32 C.F.R. 3.402(b) (1965 ed.). The regulations in effect in 1953, when the contract here involved was executed, required use of fixed price contracts for negotiated procurements "unless conditions necessitate" otherwise. 32 C.F.R. 3.401 (1954 ed.). See, also, 32 C.F.R. 3.405 (1965 ed.); 32 C.F.R. 3.405, 3.405–1, 3.406, 3406–1 (1954 ed.).

the standard default and termination-for-convenience clauses, which were included in the contract in this case (R. 244–253) although not invoked by the government. These clauses limit the contractor's recovery by reference to the contract price (see pp. 41–42, *supra*).[35] A rule of recovery that enables the contractor to disregard the contract price in recovering for his costs in excess of the contract rate stands in square conflict with this fixed-price policy preference.

At the same time, the measure of recovery prescribed by the Court of Claims frustrates the federal procurement policy of encouraging the award of contracts on the basis of competitive bids, or, where that is not feasible, of obtaining as many quotations for negotiated contracts as possible in order to secure the most advantageous terms for the government. See 10 U.S.C. 2304(g); 32 C.F.R. 3.801–1 (1965 ed.); cf. 32 C.F.R. 1.301 (1954 ed.). See, also, *Paul* v. *United States*, 371 U.S. 245, 252–253. The result of the Court of Claims' ruling is to allow Acme compensation far in excess of both its own bid and of the higher competing bids. Acme was awarded the contract, after competitive quotations were obtained, at a price of $337.23 per rifle, subject to upward or downward re-

[35] The standard default clause states that if the government's termination for default is improper because the contractor's default was excusable, or if there was no default, recovery shall be measured by the termination-for-convenience clause. 32 C.F.R. 7.103–11 (1954 ed.); 32 C.F.R. 7.103–11, 8.707 (1966 ed.). That clause specifies that the contractor is to receive the contract price for items delivered, plus its costs for uncompleted portions of the contract limited by reference to the contract price. 32 C.R.F. 7.103–21, 8.701(e) (1954 ed.); 32 C.F.R. 7.103–21, 8.701 (e) (1966).

vision, with a ceiling price of $384.95 (F. 7, R. 126–127). Other bids of $423, $484.05 and $684 per rifle were rejected (F. 7, R. 126–127). Under the Court of Claims' ruling, however, the government is to be charged Acme's costs of $1,179.29 for each of the first 446 rifles it received and $690.21 for the remaining rifles delivered prior to cancellation (F. 52, R. 206, 207–208), except to the extent that it can show these costs to have been excessive or illegal.

4. Government contracting officers have a broader duty with respect to public contracts than do private parties. A private party will repudiate his contract only if the contract appears disadvantageous. But a government officer is charged with enforcing the federal statutes and regulations designed to further important federal policies in procurement, and he may thus be authorized to cancel a contract because the contractor has violated such a statute or regulation. A breach of contract based upon an innocent but erroneous application of this principle cannot be likened to the self-interested action of a breaching private party. To impose punitive damages for a breach of the former sort is to deter government contracting officers from vigorous use of the cancellation power to foster important federal policies such as equal opportunity, honesty and fair dealing.[36]

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[36] See, *e.g.*, 10 U.S.C. 2306(b) (contingent fees); 18 U.S.C. 201–218 (bribery, graft, conflicts of interest); 28 U.S.C. 2514 (fraudulent claims); 41 U.S.C. 35, *et seq.* (Walsh-Healey Act); 41 C.F.R. 1–12.800, *et seq.*; 32 C.F.R. 12.801, *et seq.* (non-discrimination in employment); 18 U.S.C. 874 wage rebates); 41 U.S.C. 10a, *et seq.* (Buy American Act).